

**DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS: 04-0295
Indiana Corporate Income Tax
For 1999, 2000, and 2001**

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ISSUES

I. Exclusion of Taxpayer's Telemarketing Subsidiary from Taxpayer's Consolidated Indiana Income Tax Returns.

Authority: IC 6-3-2-2(l), (m); 45 IAC 3.1-1-38; 45 IAC 3.1-1-111.

Taxpayer maintains that the Department of Revenue (Department) erred when it determined that taxpayer's telemarketing subsidiary should have been included in the taxpayer's 1999, 2000, and 2001 consolidated adjusted gross income tax returns.

II. Ten-Percent Negligence Penalty.

Authority: IC 6-8.1-10-2.1; IC 6-8.1-10-2.1(d); 45 IAC 15-11-2(b); 45 IAC 15-11-2(c).

Taxpayer asks that the Department exercise its discretion to abate the ten-percent negligence penalty on the ground that any errors taxpayer made were not attributable to negligence.

STATEMENT OF FACTS

Taxpayer is an affiliated group of companies engaged in the funeral and cemetery business. Taxpayer submitted consolidated Indiana tax returns reporting its state income tax liability for 1999, 2000, and 2001. During an audit review of those returns, it was determined that taxpayer's telemarketing subsidiary should not have been included in the consolidated returns. That determination mirrored a similar decision made at the time taxpayer's 1998 return was reviewed. For each of the returns, the audit concluded that the telemarketing subsidiary did not have an Indiana nexus.

Taxpayer first protested the decision as it related to the 1998 audit. An administrative hearing was held, a Letter of Findings (LOF) was issued, taxpayer – being dissatisfied with that initial decision – asked for a rehearing, the request was granted, and a Supplemental Letter of Findings (SLOF) was issued. In that SLOF, the Department concluded that the telemarketing subsidiary was – by virtue of its part-time employees and a small amount of personal property – doing business within the state. Nevertheless, the SLOF concluded that the telemarketing subsidiary was correctly excluded from the 1998 consolidated return. The Department found that including

the telemarketing subsidiary would have the result of distorting the taxpayer's overall adjusted gross income.

Taxpayer now raises the identical issue in regards to the 1999, 2000, and 2001 returns. Taxpayer protests the audit's decision to exclude the telemarketing subsidiary from these consolidated returns. An administrative hearing was conducted during which taxpayer explained the basis for its protest, and this LOF results.

DISCUSSION

I. Exclusion of Taxpayer's Telemarketing Subsidiary from Taxpayer's Consolidated Indiana Income Tax Returns.

As one part of its funeral and cemetery business, taxpayer owns a telemarketing subsidiary. This telemarketing subsidiary operates in Indiana and in other states. In Indiana, taxpayer hires part-time employees who work out of borrowed office space. The borrowed space is provided by one of the taxpayer's other subsidiaries. The telemarketing subsidiary owns a small amount of personal property, but it does not own its own offices or other real property within the state.

The part-time employees phone Indiana residents soliciting the sale of pre-need funeral insurance policies. If a particular resident expresses interest in a pre-need funeral insurance policy, the telemarketer sends the potential customer an insurance application. The application is for an insurance policy issued by one of taxpayer's other subsidiaries; the telemarketing subsidiary does not sell these policies but cultivates consumer interest in the sale of this form of insurance. If the potential customer fills out an application, is accepted as an insured, and proceeds to make premium payments, the telemarketing subsidiary becomes entitled to a commission on the particular sale.

Therefore, telemarketing subsidiary's business consists of hiring part-time employees who facilitate the sale of insurance policies sold by a related insurance company.

As it was in the original protest, the issue is whether the Department was correct when it decided to exclude the telemarketing subsidiary from the 1999, 2000, and 2001 returns.

The information provided by taxpayer indicates that the telemarketing subsidiary had as many as 17 part-time employees during 1999. During 2000 and 2001, these 17 part-time employees were "merged with employees of Taxpayer." In late 2001, the 17 part-time employees were terminated "as the Taxpayer shifted away from pre-need marketing initiatives."

The Department is prepared to accept taxpayer's contention that the telemarketing subsidiary is "doing business" within Indiana pursuant to 45 IAC 3.1-1-38. On the basis of taxpayer's evidence, the telemarketing subsidiary "operates a business enterprise or activity in [Indiana]." 45 IAC 3.1-1-38. As a consequence of this business enterprise, the telemarketing subsidiary, "has adjusted gross income derived from sources within the state . . ." 45 IAC 3.1-1-111.

The Department has addressed the identical issue insofar as taxpayer's 1998 consolidated return. In that LOF, the Department found that although the telemarketing subsidiary had established an Indiana nexus during 1998, the telemarketing subsidiary was properly excluded from the 1998 consolidated return. The Department did so because – pursuant to IC 6-3-2-2(l), (m) – including the telemarketing subsidiary in the consolidated return would not result in a “fair, equitable, or realistic representation of taxpayer's adjusted gross income.” The Department arrived at this conclusion because including the telemarketing subsidiary in the consolidated return would permit taxpayer to “import” into its overall adjusted gross income calculation an untoward amount of the telemarketing subsidiary's federal losses thereby offsetting the entire amount of taxpayer's Indiana adjusted gross income.

In the absence of any compelling reason to do otherwise, the Department is not prepared to depart from its original conclusion that the telemarketing subsidiary's marginal business presence is sufficient to justify including the telemarketing subsidiary in the 1999, 2000, and 2001 consolidated returns.

FINDING

Taxpayer's protest is respectfully denied.

II. Ten-Percent Negligence Penalty.

Taxpayer asks that the Department abate the ten-percent negligence penalty. Taxpayer does so on the ground that it has demonstrated reasonable cause for the filing positions it has taken.

IC 6-8.1-10-2.1 requires that a ten-percent penalty be imposed if the tax deficiency results from the taxpayer's negligence. Departmental regulation 45 IAC 15-11-2(b) defines negligence as “the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer.” Negligence is to “be determined on a case-by-case basis according to the facts and circumstances of each taxpayer.” Id.

IC 6-8.1-10-2.1(d) allows the Department to waive the penalty upon a showing that the failure to pay the deficiency was based on “reasonable cause and not due to willful neglect.” Departmental regulation 45 IAC 15-11-2(c) requires that in order to establish “reasonable cause,” the taxpayer must demonstrate that it “exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed”

In regards to the 1999, 2000, and 2001 assessments, the Department agrees that taxpayer has demonstrated a reasonable basis for the positions taken.

FINDING

Taxpayer's protest is sustained.